

Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended and P.A. 71 of 1919, as amended.

Local Unit of Government Type <input type="checkbox"/> County <input type="checkbox"/> City <input type="checkbox"/> Twp <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Unit Name Hillsdale County Road Commission	County Hillsdale
Fiscal Year End December 31, 2006	Opinion Date May 4, 2007	Date Audit Report Submitted to State May 16, 2007	

We affirm that:

We are certified public accountants licensed to practice in Michigan.

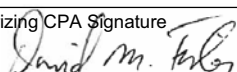
We further affirm the following material, "no" responses have been disclosed in the financial statements, including the notes, or in the Management Letter (report of comments and recommendations).

YES NO **Check each applicable box below.** (See instructions for further detail.)

1. ☒ ☐ All required component units/funds/agencies of the local unit are included in the financial statements and/or disclosed in the reporting entity notes to the financial statements as necessary.
2. ☒ ☐ There are no accumulated deficits in one or more of this unit's unreserved fund balances/unrestricted net assets (P.A. 275 of 1980) or the local unit has not exceeded its budget for expenditures.
3. ☒ ☐ The local unit is in compliance with the Uniform Chart of Accounts issued by the Department of Treasury.
4. ☒ ☐ The local unit has adopted a budget for all required funds.
5. ☒ ☐ A public hearing on the budget was held in accordance with State statute.
6. ☒ ☐ The local unit has not violated the Municipal Finance Act, an order issued under the Emergency Municipal Loan Act, or other guidance as issued by the Local Audit and Finance Division.
7. ☒ ☐ The local unit has not been delinquent in distributing tax revenues that were collected for another taxing unit.
8. ☒ ☐ The local unit only holds deposits/investments that comply with statutory requirements.
9. ☒ ☐ The local unit has no illegal or unauthorized expenditures that came to our attention as defined in the *Bulletin for Audits of Local Units of Government in Michigan*, as revised (see Appendix H of Bulletin).
10. ☒ ☐ There are no indications of defalcation, fraud or embezzlement, which came to our attention during the course of our audit that have not been previously communicated to the Local Audit and Finance Division (LAFD). If there is such activity that has not been communicated, please submit a separate report under separate cover.
11. ☒ ☐ The local unit is free of repeated comments from previous years.
12. ☒ ☐ The audit opinion is UNQUALIFIED.
13. ☒ ☐ The local unit has complied with GASB 34 or GASB 34 as modified by MCGAA Statement #7 and other generally accepted accounting principles (GAAP).
14. ☒ ☐ The board or council approves all invoices prior to payment as required by charter or statute.
15. ☒ ☐ To our knowledge, bank reconciliations that were reviewed were performed timely.

If a local unit of government (authorities and commissions included) is operating within the boundaries of the audited entity and is not included in this or any other audit report, nor do they obtain a stand-alone audit, please enclose the name(s), address(es), and a description(s) of the authority and/or commission.

I, the undersigned, certify that this statement is complete and accurate in all respects.

We have enclosed the following:	Enclosed	Not Required (enter a brief justification)		
Financial Statements	<input checked="" type="checkbox"/>			
The letter of Comments and Recommendations	<input checked="" type="checkbox"/>			
Other (Describe)	<input type="checkbox"/>			
Certified Public Accountant (Firm Name) REHMANN ROBSON		Telephone Number 517.787.6503		
Street Address 675 Robinson Road		City Jackson	State MI	Zip 49203
Authorizing CPA Signature 		Printed Name David M. Fisher, CPA		License Number 10337

Hillsdale County Road Commission

(a Component Unit of Hillsdale County)

Hillsdale, Michigan

FINANCIAL STATEMENTS

For The Year Ended December 31, 2006



REHMANN ROBSON

Certified Public Accountants

HILLSDALE COUNTY ROAD COMMISSION
(a Component Unit of Hillsdale County)

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REHMANN ROBSON

Certified Public Accountants

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INDEPENDENT AUDITORS' REPORT

May 4, 2007

Members of the Board of County
Road Commissioners
County of Hillsdale, Michigan
Hillsdale, Michigan

We have audited the accompanying financial statements of the governmental activities and the major fund of the **HILLSDALE COUNTY ROAD COMMISSION**, a component unit of Hillsdale County, Michigan, as of and for the year ended December 31, 2006, which collectively comprise the Road Commission's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of the Hillsdale County Road Commission's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and the major fund of the **Hillsdale County Road Commission** as of December 31, 2006, and the respective changes in financial position thereof and the budgetary comparison for the general fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 3-8 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements which collectively comprise the Road Commission's basic financial statements. The schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements of the **Hillsdale County Road Commission**. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

A handwritten signature in black ink, reading "Lehmann Johnson". The signature is written in a cursive, flowing style with a large initial 'L'.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Management's Discussion and Analysis

As management of the Hillsdale County Road Commission, we offer readers of the Road Commission's financial statements this narrative overview and analysis of the financial activities of this component unit of Hillsdale County, Michigan, for the fiscal year ended December 31, 2006. We encourage readers to consider the information presented herein, in conjunction with additional information that is furnished in the financial statements and notes to the financial statements.

Financial Highlights

- The County Road Commission received \$6,910,322 in revenues for our 2006 operations. Our expenditures for the year totaled \$6,360,503. This resulted in an operating surplus for the year of \$549,819. As a result, our ending operating fund balance increased to \$1,704,705. It is important to note that the fund balance includes inventories of parts and road materials that are not available to us in cash. A more realistic look at our financial status is our year-end cash and investment balance of \$732,846, which equals 11% of revenues.
- At the beginning of 2006, the Road Commission planned to operate on a closely balanced budget with a projected annual surplus of \$66,100. As the year progressed, the budget was revised in August projecting a deficit of \$165,500 with all the projects planned for the year. As winter approached, a couple of our planned gravel road projects did not get completed, and we had some other good financial news in the meantime, so the budget was last revised in December projecting a \$194,300 surplus. The final numbers reported above were even better than we expected. Our fiscal spending restraints prevented our financial status from worsening.
- In accordance with GASB 34 standards, we must annually calculate our infrastructure assets for roads, bridges and land improvements. The value of those infrastructure assets declined by \$122,312 for a year-end asset total of \$25,109,570 due to depreciation exceeding the values of our improvements in 2006, even though we had the Church Road reconstruction project.

Overview of the Financial Statements

This discussion and analysis is intended to provide a basis for understanding the Commission's financial statements. The Commission's basic financial statements comprise three components:

- 1) Government-wide financial statements
- 2) Fund financial statements
- 3) Notes to the financial statements.

To simplify financial reporting and improve readability, the government-wide financial statements and the fund statements have been combined to report the statement of net assets and general fund balance sheet on a single page and the statement of activities and general fund revenues, expenditures and changes in fund balance on a single page. This report also contains other supplementary information in addition to the basic financial statement themselves.

Government-wide Financial Statements

The statement of net assets presents information on all of the Commission's assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases or decreases in net assets may serve as an indicator of the Commission's overall financial position.

The statement of activities presents information showing how the Commission's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in past or future fiscal periods (for instance, depreciation expense associated with capital assets).

The Commission is principally supported by federal and state shared revenues (operating grants) with contributions from the townships. The governmental activities of the Commission include providing construction, repair, maintenance and snow removal of county roads within Hillsdale County. The Commission also maintains state highways within Hillsdale County under contract with MDOT.

The government-wide financial statements include only the Commission itself (known as the primary government). The Commission has no legally separate component units for which the Commission is financially accountable. In this report, financial information for this Commission is reported separately from the financial information presented for Hillsdale County which reports the Commission as a component unit.

Fund financial statements. A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Commission, like other units of state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The activity of the Commission is accounted for in a governmental fund (General Fund).

Governmental funds. *Governmental funds* (General Fund) are used to account for essentially the same functions reported in the government-wide financial statements. However, unlike the government-wide financial statements, general fund financial statements focus on *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of the general fund is narrower than that of the government-wide financial statements, it is useful to compare the information presented for the general fund with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the general fund balance sheet and the general fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between general fund and government-wide statements.

The Commission maintains one governmental fund (the General Fund). Information is presented in the general fund balance sheet and in the general fund statement of revenues, expenditures, and changes in fund balances for the Commission. The general fund is a major fund for financial reporting purposes as defined by GASB Statement #34.

The Commission adopts an annual appropriated budget for its fund and revises the same as the year progresses when needed. Budgetary comparison statements have been provided herein to demonstrate compliance with those budgets.

The Commission does not maintain proprietary nor fiduciary funds.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the Commission's financial statements. The notes are part of the basic financial statements and provide more information about the amounts in the accompanying financial statements.

Other information. In addition to the basic financial statements and accompanying notes, this report also presents certain *required supplementary information*. This is limited to this management discussion and analysis.

A presentation of the condensed Statement of Net Assets and Statement of Activities follows:

Condensed Statement of Net Assets	<u>2006</u>	<u>2005</u>
Current and Other Assets	\$ 2,218,166	\$ 1,723,588
Capital Assets	<u>28,402,094</u>	<u>28,665,725</u>
Total Assets	<u>\$ 30,620,260</u>	<u>\$ 30,389,313</u>
Long-term liabilities outstanding	(348,945)	(412,731)
Other liabilities	<u>(513,461)</u>	<u>(568,702)</u>
Total liabilities	<u>\$ (862,406)</u>	<u>\$ (981,433)</u>
Net assets:		
Invested in capital assets, net of related debt	28,402,094	28,607,313
Restricted	0	0
Unrestricted	<u>1,355,760</u>	<u>800,567</u>
Total net assets	<u>\$ 29,757,854</u>	<u>\$29,407,880</u>

Condensed Statement of Activities

Revenue

Charges for services	\$ 1,632,303	\$ 2,038,887
Operating grants & contributions	5,120,881	4,503,815
Capital grants & contributions	<u>115,147</u>	<u>592</u>
General Revenue:		
Interest income	41,991	16,653
Total Revenue	<u>\$ 6,910,322</u>	<u>\$ 6,559,947</u>

Expenses

Public Works	\$ (6,560,348)	\$ (7,330,893)
Debt Service-Principal		
Total Expenses	<u>\$ (6,560,348)</u>	<u>\$ (7,330,893)</u>

Decrease/Increase in net assets	\$ 349,974	\$ (770,946)
Net assets –beginning of year	<u>29,407,880</u>	<u>30,178,826</u>
Net assets – end of year	<u>\$ 29,757,854</u>	<u>\$ 29,407,880</u>

Capital Assets and Debt Administration

Hillsdale County Road Commission Capital Assets

	<u>2006</u>	<u>2005</u>
Land-Not depreciated	\$ 68,434	\$ 68,434
Land and improvements –Not depreciated	<u>\$ 4,241,290</u>	<u>\$ 3,932,213</u>
Buildings	1,501,231	1,564,434
Road Equipment	1,448,859	1,535,475
Shop Equipment	44,133	47,500
Office Equipment	28,146	22,805
Engineering Equipment	9,215	10,915
Yard & Storage Equipment	189,263	181,035
Depletable Assets	3,243	3,244
Infrastructure (Roads & Bridges)	<u>20,868,280</u>	<u>21,299,670</u>
Sub-Total	<u>\$ 24,092,370</u>	<u>\$ 24,665,078</u>
Total Capital Assets	<u>\$ 28,402,094</u>	<u>\$ 28,665,725</u>

Additional information on the Commission's capital assets can be found in note I-3 of the accompanying financial statements.

Long-term Debt	<u>2006</u>	<u>2005</u>
Bonds Payable	\$ 0	\$ 0
Lease Purchase Agreements	0	58,412
Compensated absences	<u>348,945</u>	<u>354,319</u>
Total	<u>\$ 348,945</u>	<u>\$ 412,731</u>

No new debt was added during the year, and the final payment of an installment lease purchase was made in 2006. Additional information on the Commission's long term debt can be found in note I-4 of the accompanying financial statements.

Economic Factors and Road Fund Budgetary Highlights

On the revenue side, our receipts from the Michigan Transportation Fund continue to decline from the highest year of 2004. We are operating with \$282,725 less per year or a loss of 6.0%. Township revenue also declined to the lowest level in 7 years, partly due to less matching money available from the Road Commission and the townships' own financial difficulties. However, the township contributions were still a healthy \$765,630 and we greatly appreciate their strong support for maintaining and improving the local road system.

Looking at the expense side of the budget, we were blessed with some good positive events that greatly reduced our expenditures. In 2006, we had a very light winter which saved us about \$60,000 in salt purchases. The light winter meant greatly reduced overtime, when coupled with the first summer season of working four 10 hour day work weeks without overtime, resulted in the lowest overtime costs in many years, and a savings of \$130,000 from the previous year. In August, we received the largest refund ever from the Michigan County Road Commission Self-Insurance Pool in the amount of \$188,536 which was almost equal to the annual premium of \$189,016. In essence, our liability and property insurance was almost free last year.

The above good news helped offset much higher costs for the materials and fuel we purchase. Our diesel fuel costs are about double what they were 4 years ago, resulting in an additional \$113,000 in 2006. Asphalt paving bids from contractors rose 33% last year from roughly \$30 per ton to \$40 per ton, which adds about \$23,000 to the cost of paving one mile of roadway. Asphalt emulsion (tar) for our sealcoating program increased from 67 cents per gallon to 98 cents per gallon, a 46% increase which added \$1,550 per mile of sealcoat. That may not seem like a lot, but multiply it by 81 miles and you have an additional cost of \$125,000. It is frustrating that road work is becoming so expensive.

The future for roads appears to be bleak for the next few years as our primary revenue sources from the state and federal governments are declining. There does not appear to be any interest from the Governor or legislators to increase the gas tax in these times of high gas prices. Also, our costs for diesel fuel, materials and asphalt paving are dramatically increasing. We will be fortunate if we can maintain our roads and bridges without a decline in their condition.

Requests for Information

This financial report is designed to provide a general overview of the Commission's finances for all those with an interest in the component unit's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Clerk, Hillsdale County Road Commission, 1919 Hudson Road, Hillsdale, MI 49242.

BASIC FINANCIAL STATEMENTS

HILLSDALE COUNTY ROAD COMMISSION

STATEMENT OF NET ASSETS AND GENERAL FUND BALANCE SHEET

DECEMBER 31, 2006

	<u>General Fund</u>	<u>Adjustments</u>	<u>Statement of Net Assets</u>
ASSETS			
Cash and cash equivalents	\$ 732,846	\$ -	\$ 732,846
Accounts receivable			
Michigan transportation funds	732,395	-	732,395
Due on county road agreements	29,500	-	29,500
Other	26,561	-	26,561
Accrued interest receivable	5,291	-	5,291
Inventories			
Road materials	547,500	-	547,500
Equipment material and parts	142,558	-	142,558
Prepaid expense	478	-	478
Deferred expense - Federal and State aid	1,037	-	1,037
Capital assets			
Assets not being depreciated	-	4,309,724	4,309,724
Assets being depreciated	-	24,092,370	24,092,370
Total assets	<u>\$ 2,218,166</u>	<u>\$ 28,402,094</u>	<u>\$ 30,620,260</u>
LIABILITIES			
Accounts payable	\$ 243,308	\$ -	\$ 243,308
Notes payable (short term)	26,756	-	26,756
Accrued liabilities	34,450	-	34,450
Escrow deposits	10,237	-	10,237
Advances	198,710	-	198,710
Long-term liabilities			
Due within one year	-	70,000	70,000
Due after one year	-	278,945	278,945
Total liabilities	<u>513,461</u>	<u>348,945</u>	<u>862,406</u>
FUND BALANCES/NET ASSETS			
Fund balances:			
Reserved for inventories	690,058	(690,058)	-
Unreserved			-
Undesignated	1,014,647	(1,014,647)	-
Total fund balances	<u>1,704,705</u>	<u>(1,704,705)</u>	<u>-</u>
Total liabilities and fund balance	<u>\$ 2,218,166</u>		
Net Assets:			
Investment in capital assets		28,402,094	28,402,094
Unrestricted		1,355,760	1,355,760
Total net assets		<u>\$ 29,757,854</u>	<u>\$ 29,757,854</u>

The accompanying notes are an integral part of these financial statements.

HILLSDALE COUNTY ROAD COMMISSION

Reconciliation of General Fund Balance Sheet to Statement of Net Assets

DECEMBER 31, 2006

Fund balances - General Fund	\$ 1,704,705
Amounts reported for <i>governmental activities</i> in the statement of net assets are different because:	
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.	28,402,094
Certain liabilities, such as compensated absences and loans payable, are not due and payable in the current period and therefore are not reported in the funds.	
Compensated absences	<u>(348,945)</u>
Net assets of governmental activities	<u>\$ 29,757,854</u>

The accompanying notes are an integral part of these financial statements.

HILLSDALE COUNTY ROAD COMMISSION

STATEMENT OF ACTIVITIES AND GENERAL FUND REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE

YEAR ENDED DECEMBER 31, 2006

	<u>General Fund</u>	<u>Adjustments</u>	<u>Statement of Activities</u>
EXPENDITURES/EXPENSES			
Current:			
Public works	\$ 6,300,914	\$ 258,257	\$ 6,559,171
Debt service			
Principal payments	58,412	(58,412)	-
Interest expense	1,177	-	1,177
	<u>6,360,503</u>	<u>199,845</u>	<u>6,560,348</u>
TOTAL EXPENDITURES/EXPENSES			
PROGRAM REVENUES			
Charges for services	1,632,303	-	1,632,303
Operating grants and contributions:			
State	5,120,881	-	5,120,881
Federal	115,147	-	115,147
	<u>6,868,331</u>	<u>-</u>	<u>6,868,331</u>
TOTAL PROGRAM REVENUES			
NET PROGRAM REVENUE			<u>307,983</u>
GENERAL REVENUES			
Interest earned	41,991	-	41,991
	<u>549,819</u>	<u>(549,819)</u>	
NET CHANGE IN FUND BALANCE			
CHANGES IN NET ASSETS		349,974	349,974
FUND BALANCE/NET ASSETS,			
Beginning of year	1,154,886	28,252,994	29,407,880
	<u>1,704,705</u>	<u>\$ 28,053,149</u>	<u>\$ 29,757,854</u>
FUND BALANCE/NET ASSETS, End of year			

The accompanying notes are an integral part of these financial statements.

HILLSDALE COUNTY ROAD COMMISSION

Reconciliation of the General Fund Revenues, Expenditures and Changes in Fund Balance to the Statement of Activities

YEAR ENDED DECEMBER 31, 2006

Net change in fund balances - General Fund	\$ 549,819
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Amounts reported for *governmental activities* in the statement of activities
are different because:

Governmental funds report capital outlays as expenditures. However, in the
statement of activities, the cost of those assets is allocated over their estimated
useful lives and reported as depreciation expense.

Add - capital outlay	515,494
Add - Infrastructure additions	1,626,672
Deduct - depreciation expense	(2,356,401)

Some expenses reported in the statement of activities do not require the use of current
financial resources and therefore are not reported as expenditures in the funds.

Equipment retirements	(49,396)
Decrease in compensated absences	5,374

Installment lease contract proceeds provide current financial resources to governmental
funds, but issuing debt increases long-term liabilities in the statement of net assets.
Repayment of debt principal is an expenditure in the funds but not in the statement
of activities:

Lease purchase installment principal payments	<u>58,412</u>
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Change in net assets of governmental activities	<u><u>\$ 349,974</u></u>
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The accompanying notes are an integral part of these financial statements.

HILLSDALE COUNTY ROAD COMMISSION
(A Component Unit of Hillsdale County)

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE -
BUDGET AND ACTUAL**

GENERAL FUND

YEAR ENDED DECEMBER 31, 2006

(With Comparative Actual Amounts for the Year Ended December 31, 2005)

	2006				2005 Actual
	Original Budget	Amended Budget	Actual	Over (Under) Amended Budget	
Revenues					
Michigan Transportation Fund	\$ 4,490,000	\$ 4,448,000	\$ 4,446,006	\$ (1,994)	\$ 4,503,560
State critical bridge fund			-	-	58
Economic development funds	700,000	674,000	674,875	875	197
Federal aid grants	115,600	115,000	115,147	147	592
Charges for services - state maintenance	641,400	552,000	547,223	(4,777)	844,060
Townships and other local units	876,600	760,000	765,630	5,630	903,889
Licenses and permits	24,000	27,000	40,057	13,057	33,138
Interest on investments	10,000	33,000	41,991	8,991	16,653
Land and building sale	-	-	-	-	750
Equipment disposals gain (loss)	188,600	218,000	214,837	(3,163)	206,264
Miscellaneous	42,000	59,000	64,556	5,556	50,786
Total revenues	7,088,200	6,886,000	6,910,322	24,322	6,559,947
Expenditures					
Primary road heavy maintenance	924,100	950,000	905,051	(44,949)	38,199
Primary road maintenance	1,705,000	1,500,000	1,425,051	(74,949)	1,729,176
Primary structures heavy maintenance	22,000	20,000	13,896	(6,104)	10,306
Primary structures maintenance	30,000	10,000	5,383	(4,617)	14,843
Local road heavy maintenance	772,600	760,000	707,414	(52,586)	891,860
Local road maintenance	2,465,200	2,270,000	2,255,572	(14,428)	2,630,156
Local structure heavy maintenance	-	3,000	312	(2,688)	4,542
Local structure maintenance	14,000	12,000	9,707	(2,293)	37,144
State trunkline maintenance	666,400	560,000	547,664	(12,336)	828,508
Equipment expenditures - net	45,000	130,000	47,407	(82,593)	(124,795)
Administrative expenditures - net	476,000	492,000	479,692	(12,308)	441,758
Capital outlay - net	(199,000)	(120,000)	(141,319)	(21,319)	144,820
Debt service	60,800	59,700	59,589	(111)	79,449
Other operating expenditures	40,000	45,000	45,084	84	20,663
Total expenditures	7,022,100	6,691,700	6,360,503	(331,197)	6,746,629
Net change in fund balance	66,100	194,300	549,819	355,519	(186,682)
Fund balance, beginning of year	1,154,886	1,154,886	1,154,886	-	1,341,568
Fund balance, end of year	\$ 1,220,986	\$ 1,349,186	\$ 1,704,705	\$ 355,519	\$ 1,154,886

The accompanying notes are an integral part of these financial statements.

HILLSDALE COUNTY ROAD COMMISSION

NOTES TO FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the Hillsdale County Road Commission (the “Road Commission”) conform to generally accepted accounting principles as applied to governmental units. The following is a summary of the significant policies.

Reporting Entity

The Hillsdale County Road Commission, referred to as the Road Commission, is a discrete component unit of the County of Hillsdale, Michigan. The Road Commission was established pursuant to the county road law (MCL 224.1), and is governed by a three member Board of County Road Commissioners elected by Hillsdale County voters.

The criteria established by the Governmental Accounting Standards Board Statement No. 14, “The Financial Reporting Entity”, for determining the reporting entity includes having financial accountability. Based on the above criteria, these financial statements present the Hillsdale County Road Commission, a discretely presented component unit of Hillsdale County, and include the Road Commission General Operating Fund.

The Road Commission General Operating Fund is used to control the expenditures of Michigan Transportation Fund monies distributed to the County, which are earmarked by law for street and highway purposes. The Board of County Road Commissioners has responsibility for the administration of the Road Commission’s General Operating Fund.

Basis of Presentation

Government-wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the activities of the primary government. *Governmental activities* are supported by charges for services and intergovernmental revenues.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. *Direct expenses* are those that are clearly identifiable with a specific function or segment. *Program revenues* include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Internally dedicated resources are reported as general revenues rather than as program revenues.

As permitted by GASB Statement No. 34, the Road Commission uses an alternative approach reserved for single program governments to present combined government-wide and fund financial statements by using a columnar format that reconciles individual line items of fund financial data to government-wide data in a separate column. Accordingly, this is presented in the Statement of Net Assets and Governmental Funds Balance Sheet and the Statement of Activities and Governmental Fund Revenues, Expenditures and Changes in Fund Balances. The general fund, the sole major governmental fund, is reported as a separate column in the aforementioned financial statements.

HILLSDALE COUNTY ROAD COMMISSION

NOTES TO FINANCIAL STATEMENTS

Measurement Focus Basis of Accounting and Financial Statement Presentation

The government-wide financial statements (statement of net assets and the statement of activity) are reported using the *economic resources measurement focus* and the *accrual basis of accounting*. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund (general fund) financial statements (general fund balance sheet and general fund revenues, expenditures and changes in fund balance) are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences not expected to be paid in the current year and claims and judgments, are recorded only when payment is due.

State and grant revenue, licenses and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the government.

The government reports the following major governmental fund:

The *general fund* is the government's primary operating fund. It accounts for all financial resources of the general government.

Budgetary Data

The governmental fund is under formal budgetary control. Budgets shown in the financial statements are adopted on a basis consistent with generally accepted accounting principles (GAAP), and are not significantly different from the modified accrual basis used to reflect actual results, and consist only of those amounts contained in the formal budget as originally adopted or amended by the Board of County Road Commissioners. The budget for the general operating fund is adopted on a functional level basis. Budget variances at the functional level, if any, are disclosed on the Statement of Revenues, Expenditures and Changes in Fund Balance - Budget and Actual.

HILLSDALE COUNTY ROAD COMMISSION

NOTES TO FINANCIAL STATEMENTS

Inventory

Inventory consists of various operating parts, supplies, and road material, and the cost is recognized using the consumption method (inventories recorded as expenditures when they are used). Inventories are stated at average cost determined on a first-in, first-out method, except for road materials, which are determined on the average cost method, and are not in excess of fair value.

Fund Balance Reservations and Designations

Portions of fund equity are segregated for future use, and are, therefore, not available for future appropriation. Amounts are reserved for inventories for monies already spent to show the amount of fund balance not currently available for expenditures. Designations of unreserved fund balances in governmental funds indicate the Road Commission's intention to use this portion of fund balance in the subsequent year.

Capital Assets

Capital assets, which include property, equipment and infrastructure assets (roads, bridges and similar items) are reported in the government-wide statements. In 2004, the Road Commission began capitalizing and depreciating infrastructure assets as indicated on the government-wide statements. Capital assets are defined by the Road Commission as assets with an initial cost of \$200 or more and an estimated life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date donated.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized.

Capital assets are recorded as capital expenditures at the time of purchase in the fund financial statements and are subsequently capitalized on the government-wide statements through an adjustment to the governmental fund (general fund) column.

The Uniform Accounting Procedures prescribed for Michigan County Road Commissions provide for recording depreciation in the General Operating Fund as a charge to various expense accounts and a credit to the depreciation contra expense account. Accordingly, the annual depreciation expense does not affect the available operating fund balance of the General Operating Fund.

Depreciation is recorded over the estimated useful lives (ranging from five to fifty years) of the assets, using the sum-of-years digits method for road equipment and straight-line method for all other capital assets and infrastructure as follows:

<u>Asset Category</u>	<u>Useful Life in Years</u>
Buildings and improvements	40
Equipment	4 to 8
Infrastructure	8 to 50

HILLSDALE COUNTY ROAD COMMISSION

NOTES TO FINANCIAL STATEMENTS

Deferred Compensation Plan

The Road Commission offers its employees a deferred compensation plan created in accordance with IRS section 457. The plan, available to all Commission employees, permits them to defer a portion of their current salary until future years. A trust has been established for the plan assets and the related assets and liability are not included in the Road Commission's financial statements.

Long-term Obligations

In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities. Bond premiums and discounts are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable bond premium or discount. As permitted by GASB Statement No. 34, the Road Commission has elected to apply the provisions related to bond premiums, discounts, and issuance costs on a prospective basis.

Compensated Absences

Under existing general Road Commission rules and regulations and its Labor Agreement, all regular full-time employees are eligible for paid leave in varying amounts based on number of years of service completed by each employee as of the preceding calendar year.

Sick leave is accumulated, for employees with one year or more of service, at the rate of one day for each month of service, not to exceed a total accumulation of 60 days. Accumulated sick pay at 100% is payable to employees upon death or retirement and 50% for employees who quit or are discharged.

Accumulated vacation pay is payable 100% to employees in case of retirement, resignation, discharge or death.

2. CASH AND CASH EQUIVALENTS

Deposits

At December 31, 2006, the amount of the Road Commission's deposits were as follows:

	<u>Carrying Amount</u>	<u>Bank Balance</u>
Petty cash	\$ 100	\$ -
Held by Hillsdale County*		
Checking	1,135	56,805
Liquid savings accounts	631,611	634,481
Certificates of deposit	100,000	100,000
	<u>\$ 732,846</u>	<u>\$ 791,286</u>

HILLSDALE COUNTY ROAD COMMISSION

NOTES TO FINANCIAL STATEMENTS

*Deposits of the Road Commission held by Hillsdale County may be partially covered by federal depository insurance. The amount of federal depository insurance is determined for the County as a whole, but cannot be separately identified for the Road Commission.

Statutes authorize the Road Commission to invest funds in the following:

- Bonds, securities, other obligations and repurchase agreements of the United States, or an agency or instrumentality of the United States
- Certificates of deposit, savings accounts, deposit accounts or depository receipts of a qualified financial institution
- Commercial paper rated at the time of purchase within the 2 highest classifications established by not less than 2 standard rating services and that matures not more than 270 days after the date of purchase
- Bankers acceptances of United States banks
- Obligations of the State of Michigan and its political subdivisions that, at the time of purchase are rated as investment grade by at least one standard rating service
- Mutual funds registered under the investment company act of 1940 with the authority to purchase only investment vehicles that are legal for direct investment by a public corporation
- External investment pools as authorized by Public Act 20 as amended through 12/31/97

Investment and deposit risk

Interest Rate Risk. State law limits the allowable investments and the maturities of some of the allowable investments as identified in the listing of authorized investments above. The Road Commission's investment policy does not have specific limits in excess of state law on investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. The Road Commission has no investments at December 31, 2006.

Credit Risk. State law limits investments to specific government securities, certificates of deposits and bank accounts with qualified financial institutions, commercial paper with specific maximum maturities and ratings when purchased, bankers acceptances of specific financial institutions, qualified mutual funds and qualified external investment pools as identified in the list of authorized investments above. The Road Commission's investment policy does not have specific limits in excess of state law on investment credit risk. The Road Commission has no investments at December 31, 2006.

Custodial Credit Risk – Deposits. Custodial credit risk is the risk that in the event of a bank failure, the Road Commission's deposits may not be returned. State law does not require and the Road Commission does not have a policy for deposit custodial credit risk. As of December 31, 2006, deposits in the amount of \$791,286 held by Hillsdale County may be partially covered by federal depository insurance. The amount of federal depository insurance is determined for the County as a whole, but cannot be separately identified for the Road Commission.

HILLSDALE COUNTY ROAD COMMISSION

NOTES TO FINANCIAL STATEMENTS

Custodial Credit Risk – Investments. For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Road Commission will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. State law does not require and the Road Commission does not have a policy for investment custodial credit risk.

Concentration of Credit Risk. State law limits allowable investments but does not limit concentration of credit risk as identified in the list of authorized investments above. The Road Commission's investment policy does not have specific limits in excess of state law on concentration of credit risk. The Road Commission has no investments at December 31, 2006,

3. CAPITAL ASSETS

Changes in the components of the capital assets are summarized as follows:

	Balance January 1, 2006	Additions	Deductions	Adjustments and Reclassifications	Balance December 31, 2006
Capital assets not being depreciated:					
Land	\$ 68,434	\$ -	\$ -	\$ -	\$ 68,434
Land improvements - infrastructure	3,932,213	309,077	-	-	4,241,290
Subtotal	4,000,647	309,077	-	-	4,309,724
Capital assets being depreciated:					
Buildings and improvements	2,029,524	-	-	(945)	\$ 2,028,579
Road equipment	5,596,712	468,741	532,927	945	5,533,471
Shop equipment	95,495	4,859	962	1,221	100,613
Office equipment	136,346	12,639	-	(1,692)	147,293
Engineers' equipment	56,376	3,100	-	471	59,947
Yard and storage	426,965	26,155	16,585	-	436,535
Depletable assets	65,400	-	-	-	65,400
Infrastructure	41,291,298	1,317,595	-	-	42,608,893
Subtotal	49,698,116	1,833,089	550,474	-	50,980,731
Accumulated depreciation and depletion					
Buildings and improvements	465,090	62,361	-	(103)	527,348
Equipment	4,514,164	545,055	501,078	103	4,558,244
Depletable assets	62,156	-	-	-	62,156
Infrastructure	19,991,628	1,748,985	-	-	21,740,613
Total accumulated depreciation and depletion	25,033,038	2,356,401	501,078	-	26,888,361
Total capital assets being depreciated - net	24,665,078	(523,312)	49,396	-	24,092,370
Governmental activities capital assets - net	\$ 28,665,725	\$ (214,235)	\$ 49,396	\$ -	\$ 28,402,094

HILLSDALE COUNTY ROAD COMMISSION

NOTES TO FINANCIAL STATEMENTS

4. LONG-TERM DEBT

Long-term debt of the Road Commission consists of the following:

	Balance January 1, 2006	Increases	Decreases	Balance December 31, 2006	Due Within One Year
Installment lease purchase	\$ 58,412	\$ -	\$ 58,412	\$ -	\$ -
Compensated absences	354,319	-	5,374	348,945	70,000
	<u>\$ 412,731</u>	<u>\$ -</u>	<u>\$ 63,786</u>	<u>\$ 348,945</u>	<u>\$ 70,000</u>

The installment lease purchase agreement was paid in full.

Also, during the year advances from the State Department of Transportation for the State Trunkline Maintenance contract were increased by \$1,841. Total advances are \$198,396 as of December 31, 2006.

5. RETIREMENT PLAN

Plan Description

The Road Commission's defined benefit pension plan provides retirement and disability benefits and death benefits to plan members and beneficiaries. The Road Commission participates in the Municipal Employees Retirement System of Michigan (MERS), an agent multiple-employer plan administered by the MERS Retirement Board. Act No. 427 of the Public Acts of 1984, as amended, establishes and amends the benefit provisions of the participants in MERS. The Municipal Employees Retirement System of Michigan issues a publicly available financial report that includes financial statements and required supplementary information for MERS. That report may be obtained by writing to the Municipal Employees Retirement System of Michigan, 1134 Municipal Way, Lansing, Michigan 48917, or by calling (800) 767-6377.

Funding Policy

The Road Commission is required to contribute at an actuarially determined rate; the current employer's contribution rate of annual covered payroll is 7.25% for Association members and 11.07% for non-Association members. The contribution requirements of the Road Commission are established by Act No. 427 of the Public Acts of 1984, as amended, and may be amended by the Retirement Board of MERS. The contribution requirements of plan members, if any, are established and may be amended by the Road Commission. In addition, Road Commission Association employees are required to contribute 5.3% of annual compensation, and non-Association 9.9%.

HILLSDALE COUNTY ROAD COMMISSION

NOTES TO FINANCIAL STATEMENTS

Annual Pension Cost

For the year ended December 31, 2006, the Road Commission's annual pension cost of \$151,739 for MERS was equal to the Road Commission's required and actual contributions. The required contribution was determined using the entry age actuarial cost method. The actuarial assumptions included (a) a rate of return on the investment of present and future assets of 8.0%, (b) projected salary increase of 4.5% per year compounded annually, attributable to inflation, and (c) additional projected salary increases of 0.0% to 4.50% per year, depending on age, attributable to seniority/merit. The actuarial value of MERS assets was determined on the basis of a valuation method that assumes the fund earns the expected rate of return, and includes an adjustment to reflect market value. The Road Commission's unfunded actuarial accrued liability is being amortized as a level percentage of projected payroll on an open basis. The remaining amortization period at December 31, 2005, the date of the latest actuarial report, was 30 years.

Three-Year Trend Information

<u>Fiscal Year Ending</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
12/31/04	\$ 123,395	100%	\$ -
12/31/05	146,018	100	-
12/31/06	151,739	100	-

Schedule of Funding Progress

<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets</u>	<u>Actuarial Accrued Liability (AAL) - Entry Age</u>	<u>Unfunded Actuarial Liability (UAAL)</u>	<u>Funded Ratio</u>	<u>Covered Payroll</u>	<u>UAAL as a Percentage of Covered Payroll</u>
12/31/03	\$ 3,364,902	\$ 4,649,366	\$1,284,464	72%	\$ 1,871,340	69%
12/31/04	3,660,821	6,055,828	2,395,007	60	1,890,184	126
12/31/05	4,028,654	6,292,619	2,263,965	64	1,893,260	120

HILLSDALE COUNTY ROAD COMMISSION

NOTES TO FINANCIAL STATEMENTS

6. RISK MANAGEMENT

The Road Commission is a member of the Michigan County Road Commission Self-Insurance Pool "Pool" established pursuant to the laws of the State of Michigan which authorizes contracts between municipal corporations (inter local agreements) to form group self-insurance pools, and to prescribe conditions to the performance of these contracts.

The Michigan County Road Commission Self-Insurance Pool was established for the purpose of making a self-insurance pooling program available for Michigan County Road Commissions, which includes, but is not limited to, general liability coverages, auto liability coverages, property insurance coverages, stop loss insurance protection, claims administration, and risk management and loss control services pursuant to Michigan Public Act 138 of 1982.

The Hillsdale County Road Commission pays an annual premium to the Pool for general liability, excess liability, errors and omissions, auto liability, auto comprehensive, auto collision, equipment and building and contents.

The agreement for the formation of the Pool provides that the Pool will be self-sustaining through member premiums and will purchase both specific and aggregate stop-loss insurance to the limits determined necessary by the Pool Board.

The Road Commission continues to carry commercial insurance for all other risks of loss, including life, health, and workers' compensation insurances. Settled claims have not exceeded insurance coverage for the last three years.

7. CONTINGENCIES

Under the terms of various Federal and State grants, periodic audits are required and certain costs may be questioned as not being appropriate expenditures under the terms of the grants. Such grants could lead to reimbursement to the grantor agencies. However, Road Commission management does not believe such disallowances, if any, will be material to the financial position of the Road Commission.

* * * * *

OPERATING FUND SCHEDULES

HILLSDALE COUNTY ROAD COMMISSION
(A Component Unit of Hillsdale County)

SCHEDULE OF CHANGES IN FUND BALANCES

YEAR ENDED DECEMBER 31, 2006

	Primary Road Fund	Local Road Fund	County Road Commission	Totals
Total revenue	\$ 3,525,567	\$ 2,497,044	\$ 887,711	\$ 6,910,322
Total expenditures	<u>2,574,957</u>	<u>3,268,436</u>	<u>517,110</u>	<u>6,360,503</u>
Revenue over (under) expenditures	950,610	(771,392)	370,601	549,819
Optional transfers and adjustments	<u>(771,392)</u>	<u>771,392</u>	<u>-</u>	<u>-</u>
Revenue over transfers and adjustments	179,218	-	370,601	549,819
Fund balance, beginning of year	<u>683,060</u>	<u>-</u>	<u>471,826</u>	<u>1,154,886</u>
Fund balance, end of year	<u><u>\$ 862,278</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 842,427</u></u>	<u><u>\$ 1,704,705</u></u>

HILLSDALE COUNTY ROAD COMMISSION**(A Component Unit of Hillsdale County)****SCHEDULE OF REVENUES****YEAR ENDED DECEMBER 31, 2006**

	Primary Road Fund	Local Road Fund	County Road Commission	Totals
State Aid:				
Michigan Transportation Fund				
Engineering	\$ 6,100	\$ 3,900	\$ -	\$ 10,000
Allocation	2,601,169	1,728,975	-	4,330,144
Urban roads	75,365	28,166	-	103,531
Snow removal	1,422	909	-	2,331
Economic Development Fund				
Federal aid buy out	674,875	-	-	674,875
	<u>3,358,931</u>	<u>1,761,950</u>	<u>-</u>	<u>5,120,881</u>
Federal Aid:				
STP	115,147	-	-	115,147
Charges for Services				
State trunkline maintenance	-	-	538,808	538,808
State trunkline nonmaintenance	-	-	8,415	8,415
	<u>-</u>	<u>-</u>	<u>547,223</u>	<u>547,223</u>
Contributions:				
Township, City, Private	30,536	735,094	-	765,630
Other Revenue:				
Salvage sales	-	-	7,802	7,802
Interest earned	20,953	-	21,038	41,991
Permit and inspection fees	-	-	40,057	40,057
Gain on equipment disposal	-	-	214,837	214,837
Other miscellaneous	-	-	56,754	56,754
	<u>20,953</u>	<u>-</u>	<u>340,488</u>	<u>361,441</u>
Total Revenue	<u><u>\$ 3,525,567</u></u>	<u><u>\$ 2,497,044</u></u>	<u><u>\$ 887,711</u></u>	<u><u>\$ 6,910,322</u></u>

HILLSDALE COUNTY ROAD COMMISSION
(A Component Unit of Hillsdale County)

SCHEDULE OF EXPENDITURES

YEAR ENDED DECEMBER 31, 2006

	<u>Primary Road Fund</u>	<u>Local Road Fund</u>	<u>County Road Commission</u>	<u>Totals</u>
Primary Road				
Heavy Maintenance	\$ 905,051	\$ -	\$ -	\$ 905,051
Maintenance	1,425,051	-	-	1,425,051
Local Road				
Heavy Maintenance	-	707,414	-	707,414
Maintenance	-	2,255,572	-	2,255,572
Primary Road Structure				
Heavy Maintenance	13,896	-	-	13,896
Maintenance	5,383	-	-	5,383
Local Road Structure				
Heavy Maintenance	-	312	-	312
Maintenance	-	9,707	-	9,707
State Trunkline Maintenance and Non-maintenance	-	-	547,664	547,664
Equipment Expense - Net	13,833	27,482	6,092	47,407
Administrative Expense - Net	211,743	267,949	-	479,692
Capital Outlay - Net	-	-	(141,319)	(141,319)
Debt Service - Principal	-	-	58,412	58,412
- Interest	-	-	1,177	1,177
Other Expenditures	-	-	45,084	45,084
Total Expenditures	<u><u>\$ 2,574,957</u></u>	<u><u>\$ 3,268,436</u></u>	<u><u>\$ 517,110</u></u>	<u><u>\$ 6,360,503</u></u>



REHMANN ROBSON

Certified Public Accountants

A member of THE REHMANN GROUP



May 4, 2007

To the Board of County Road Commissioners of the
Hillsdale County Road Commission
Hillsdale, Michigan

We have audited the financial statements of Hillsdale County Road Commission, a component unit of Hillsdale County, as of and for the year ended December 31, 2006, and have issued our report thereon dated May 4, 2007. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility Under Auditing Standards Generally Accepted in the United States of America

As stated in our engagement letter dated April 4, 2007, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement and are fairly presented in accordance with accounting principles generally accepted in the United States of America. Because an audit is designed to provide reasonable, but not absolute assurance and because we did not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by us.

As part of our audit, we considered the internal control of Hillsdale County Road Commission. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

Significant Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we advised management about the appropriateness of accounting policies and their application. The significant accounting policies used by Hillsdale County Road Commission are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year. We noted no transactions entered into by Hillsdale County Road Commission during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were:

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- Management's estimate of the useful lives of depreciable fixed assets is based on the length of time it is believed that those assets will provide some economic benefit in the future. We evaluated the key factors and assumptions used to develop the useful lives of those assets in determining that they are reasonable in relation to the financial statements taken as a whole.

Audit Adjustments

For purposes of this letter, professional standards define an audit adjustment as a proposed correction of the financial statements that, in our judgment, may not have been detected except through our auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on Hillsdale County Road Commission's financial reporting process (that is, cause future financial statements to be materially misstated). In our judgment, none of the adjustments we proposed, whether recorded or unrecorded by Hillsdale County Road Commission, either individually or in the aggregate, indicate matters that could have a significant effect on Hillsdale County Road Commission's financial reporting process.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Issues Discussed Prior to Retention of Independent Auditors

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as Hillsdale County Road Commission's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Difficulties Encountered in Performing the Audit

We encountered no difficulties in dealing with management in performing our audit.

This letter is intended for the use of the Board of County Road Commissioners, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

A handwritten signature in black ink, appearing to read "Lehmann Lohman". The signature is written in a cursive, flowing style.

Hillsdale County Road Commission

Comments and Recommendations

For the Year Ended December 31, 2006

In planning and performing our audit of the financial statements of Hillsdale County Road Commission, a component unit of Hillsdale County, as of and for the year ended December 31, 2006, in accordance with auditing standards generally accepted in the United States of America, we considered the Commission's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Commission's internal control. Accordingly, we do not express an opinion on the effectiveness of the Commission's internal control.

Our consideration of internal control was for the limited purpose described in the first paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We noted no matters we consider to be control deficiencies.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control was for the limited purpose described in the first paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control that we consider to be material weaknesses, as defined above.

* * * * *